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C O N F I D E N T I A L SECTION 01 OF 02 RANGOON 000225

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STATE FOR EAP/BCLTV, EB
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USPACOM FOR FPA

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TAGS: EFIN PREL ECON BM
SUBJECT: BURMA'S BANKS: GOB TAKES ACTION, BUT IS IT ENOUGH?

REF: A. RANGOON 214
¶B. RANGOON 213

Classified By: CDA a.i. Ron McMullen for Reasons 1.5 (B,D)

¶1. (C) Summary: The GOB has agreed to extend loans beginning next week to the country's beleaguered private banking sector. However, the regime blames the banks for their predicament, and has apparently decided to let the crisis run its course without trying any extraordinary new steps to reassure depositors. Hectic efforts by bankers to lure back customers, combined with some short term measures allowing banks access to their reserves at the Central Bank, are keeping the peace for now. Next week will be a test for this approach, however, as almost all companies in the country have to meet payroll obligations on February 28. If employees are not paid that day, there could be trouble. End summary.

Turning the Corner?

¶2. (C) There was some optimism on February 20 that the banking crisis here had "turned the corner." This sentiment, apparently stemming from an analysis sent to Senior General Than Shwe, is based on an agreement between the government and stricken private banks for the Central Bank to advance an undisclosed amount of money to the banks within a week. This new money, hot of the presses, will be collateralized by the real assets now being used as collateral for the banks' outstanding loans. Reportedly the Finance Ministry has also demanded that each of the private banks' chairmen put up their own residence as part of the collateral.

¶3. (C) In the meantime, the GOB has allowed banks to draw from their reserves on deposit at the Central Bank. Thus far AWB has drawn "several billion" kyat by converting many of the GOB bonds it held in the Central Bank. Yoma Bank has taken about 5 billion kyat (roughly $5 million at current rates). Other banks have drawn or will reportedly draw an estimated 1 to 2 billion kyat per institution. These draw downs will not come close to matching the outflow thus far, however, which is estimated at more than 200 billion kyat ($200 million; with AWB and Yoma Banks losing 120 billion and 60 billion kyat respectively). That total is equivalent to about 40 percent of the banks' total deposits (now reported as about 550 billion kyat) and virtually all of their cash on hand at the start of the crisis.

¶4. (C) The hardest hit banks now are still relying on emergency measures to keep themselves afloat until the Central Bank advances are organized and paid out. According to the Yoma Bank chairman, these measures include stopping all new lending, including credit card operators; calling in whatever loans it can; offering "guaranteed" accounts; and an advertising campaign urging customers to return deposits of any amount. In addition, the banks are continuing to ration out weekly withdrawals. Currently Yoma Bank and others are handing out chits to customers supposedly entitling them to a withdrawal (currently 100,000 kyat) several days in the future.

GOB: "Let Them Stew in Their Own Wine"

¶5. (C) For now we do not expect the GOB to take any more aggressive or strategic action to aid the banks in returning confidence -- and deposits. Economic journalists and bankers with whom we spoke have all agreed that the top decisionmakers here (read: Vice Senior General Maung Aye and Senior General Than Shwe) still view the banks' problems as their just reward for flouting the law with shady deals. "Let them stew in their own wine," is one reported comment by Maung Aye. The SPDC leadership has long been reported to dislike the private banking sector (or at least some members of it) because it is "politically uncontrollable." Unfortunately, the consequences of the regime's actions, if they prove inadequate, will be felt by all twenty private banks, even though the junta's ire (and current crisis) was apparently provoked by the actions of only a few bankers.

All Quiet...For Now

¶6. (C) The combination of measures the banks have put in place seems to be working for now. Crowds have dispersed from in front of bank branches, and there have been no further reports of stone throwing or other civil disorder. Presumably individual depositors will remain calm as long as there is some credible promise of payment and some hope to recover their funds. If the banks get the transfusion they need from the Central Bank, matters may sort themselves out. Some business people, in fact, are confident that the lines of credit will restore enough liquidity to get commerce, largely frozen since February 18, moving again.

¶7. (C) Because those with kyat are holding tight in case of further emergency, asset prices have been dropping rapidly. The price of gold has dropped 35 percent since February 14 and the dollar has fallen to 950 kyat/dollar (after dipping to 800 kyat/dollar briefly on February 19). This trend should reverse in the short term if confidence is restored. However, we may not see a return to the same rates of general inflation and kyat depreciation that prevailed before the crisis. One healthy result of the this crisis has been to purge the economy of the uncontrolled credit creation system run by the informal financial system. With hindsight, it now appears that their operations might have accounted for as much as half of the credit creation and half the inflation that plagued Burma over the past three years. Provided the Central Bank retires its advances to the banking system as customers return their deposits, not at all a sure thing, overall inflation in Burma could settle to levels much lower than we have witnessed over the past several years.

How Long Can the Peace Hold?

¶8. (C) The coming week will test the current government strategy. In particular there are two dates looming that might exacerbate the situation. First, Senior General Than Shwe is scheduled to leave for Malaysia this weekend. As he is the sole arbiter of policy, should a downturn occur early next week the GOB will likely be paralyzed. Second, pay day across the country for many wage earners is February 28. If a significant number of employers are unable to meet payroll, there could be some serious consequences.
McMullen